

**PROPERTY TAXATION
IN MONTANA**

**A REPORT TO THE THIRTY-SEVENTH
LEGISLATIVE ASSEMBLY**

by the

**Montana Legislative Council
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THE STATE BOARD AS A BOARD OF APPEALS

Persons who have appealed their assessment to the county board of equalization and are "aggrieved by the action of any county board of equalization", can appeal to the state board of equalization by filing notice of appeal with both the county and state boards within ten days of the county board's action. The state board must give appellants at least five days' notice of time and place of the hearing. The board may assign the hearing of the appeal to "one of its members, to its secretary, counsel or chief auditor" and make its determination from the records of the proceedings.

The board also hears "appeals" from taxpayers which the board itself has assessed.

In 1959 fifteen appeals from county boards of equalization were begun. Hearings were held on eleven of these. Five appeals were granted; six were denied.

ASSESSMENT

The board also acts as an assessing agency, where some inter-county properties are concerned. Chapter IV covers this subject thoroughly.

PROBLEMS OF ASSESSMENT

Two major and almost universal problems of property tax administration are underassessment and the absence of uniform assessments.

Underassessment arises when property is assessed at less than the level required by statute. Several states allow assessing jurisdictions to establish their own level of assessment. Where this is the case, there is no problem of underassessment.

Assessment uniformity exists when all classes of property within a taxing jurisdiction are assessed at the same level. Since the amount of property tax paid is determined directly by the value of property, the equity of the tax depends upon the degree of success taxing jurisdictions achieve in arriving at like assessments for properties of equal market value.

The Problem of Underassessment

Nearly $\frac{3}{4}$ of the states require assessment of property at market value. Nine other states define a specific percentage of market value at which property is to be assessed. Sales assessment ratio studies conducted by the Bureau of Census during a six-months period in 1956 revealed that all states, including those that recently have established fractional assessment levels in an effort to legalize existing levels of underassessment, fell short of the statutory level of assessment on real property.

Montana's statutes require that all taxable property be assessed at its "full cash value". The Census shows Montana's assessment of real property as 8% of its value as indicated by sales prices; however, this figure was determined by using taxable value rather than assessed value. The figure reflects, therefore, not only the performance of the assessor but the effects of our property classification law as well. The combination of underassessment and our classification law means that mill levies are applied to only about 8% of the market value of real estate.

The performance of the assessors can be more accurately demonstrated by adjusting the census figures to show assessed values as a percent of sales prices. This reveals that in Montana non-farm residential property is assessed from 28.7 to 31.7% of its sales value; farm real estate is assessed from 22.7 to 23.3% of its sales value.⁴

⁴U. S. Dept. of Commerce, Bureau of Census, 1957 *Census of Governments*, Vol. V, *Taxable Property Values in the United States*, 1959, p. 28-29.

Assessment of non-farm residential property in the United States as a whole was slightly less than 32% of market value. The national average for farm real property was slightly more than 20%. Thus, Montana's assessments for non-farm and farm realty are close to the national averages. Rhode Island, with more than 61% for non-farm and about 50% for farm real estate, had the highest assessment level in the nation.

There are several reasons why assessments do not reveal a closer compliance with the law. Assessments are naturally slow to respond to rapid changes in the general price level. This lag of assessments is revealed in Graphs 3, 4, and 5 in Chapter II of this report. In the 1920's assessments of farm lands were somewhat less than market value. During the depression years a decline in real estate values coupled with relatively static assessments brought the assessment level up to, and in the case of grazing land above, market value. Since then a combination of price increases and static assessments have reduced the level of assessment to new lows. Within limits, this "stickyness" of assessments is understandable. Assessment rolls cannot be adjusted overnight, and assessors have to be sure that price changes are not going to be of short duration. The degree of underassessment in recent years may, to some extent, reflect the unwillingness of some assessors to accept present day prices for real estate as reflecting a lasting or "normal" price trend.⁵

But there is more to underassessment than a natural lag. The assessor's temptation to underassess also helps explain the prevalence of noncompliance with legal requirements. Where the state imposes a property tax levy or where state aid to schools is apportioned on the basis of yields from fixed mill levies, assessors are under considerable pressure to compete among themselves for underassessment. By assessing at less than the average level, the county assessor can shift state property taxes to other counties and increase apparent need for state aid to schools.

Even where state levies and school aid programs are not factors, there are elements inherent in the assessor's position which pressure him to underassess. The assessor, who among all local officials receives the most complaints about taxes, can use underassessment to parry them. Because the individual will often consider himself as having received a "break", underassessment is popular with property owners. This is an important consideration to a man who must retain his office through election. Moreover, by covering up the lack of uniform assessments, fractional assessments can be a source of comfort to the assessor; the property owner who is assessed at considerably less than the required level is unlikely to protest his assessment even though other property may be assessed at lesser percentages of the assessment standard.

Through its misdirected hostility to taxes, the public places the assessor, and other local taxing officials as well, in a difficult position. Since neither the assessor nor local legislative bodies want to appear responsible for any tax increases, a situation of stress is created between them. The assessor may wish to keep assessments in line with price increases, but he knows that if he does so and local governing agencies fail to decrease mill levies, protest as he might, he will probably incur public wrath for tax increases. If he can hold the line on assessments and local legislative bodies are forced to resort to increased mill levies, responsibility for tax increases will be shifted to them. The assessor, thus, is faced with two alternatives: he can administer his office as required by law, and court political martyrdom, or he can abide by existing practices and perhaps place some of his troubles in someone else's lap.

⁵ An extreme example of assessment "stickyness" emerged during a hearing before the Lewis and Clark County Board of Equalization, where it was revealed that assessment increases on some vacant lots were the first since 1885. Helena Independent Record, August 3, 1960, p. 3.

SOME EFFECTS OF UNDERASSESSMENT

Underassessment has some undesirable effects which are not immediately obvious.⁶ Underassessment transforms the office of assessor from a technical and administrative position to a legislative office. For example, in Montana salaries of many local officials are tied by statute to population and taxable valuation of counties. By assessing at less than the legal limit, the assessor alters the effect of these statutes and reduces the salaries of some officials. Similarly, fractional assessments also alter existing statutory taxing and bonding limitations by making them more restrictive than contemplated by law. This misrepresents the fiscal capacities of local governments and leaves some of them with little or no financial elbow room.

Drastic underassessment also transfers some of the budgetary powers of county commissioners and city and school district officials to the county assessor. This situation has been described as follows:

Fractional assessment has the added evil of completely upsetting a normal political process of local budgetary determination. After a unit of government has reached its maximum rate limitation, its future budgetary policy is largely in the hands of the assessor. The decision made in his office as to the percentage of market value that will be used for assessment purposes is almost controlling. Moreover, decisions made by the assessor are more apt to be influenced by consideration of his political future than by the legitimate revenue needs of local government. Thus we have the spectacle of the county assessor, whose sole function is to find and value property at its full value, charting the fiscal policy of most local governments.⁷

Testimony before the Montana Governor's Special Committee on Taxation in 1955 revealed how some assessors have assumed the role of "budget watchdogs". Assessors who testified expressed the fear that if they were to assess at higher levels, mill levies would not be reduced proportionately. The result would be higher tax bills. They felt they could stave off this eventuality by keeping assessments down.

Furthermore, the 1957 Census of Governments presents some evidence of a correlation between underassessment and a lack of uniform assessments within assessment jurisdictions. The Census' measurement of the extent of assessment inequality for non-farm houses in sample areas revealed "that inequality of assessments tends to increase as the level of assessment declines."⁸

It is not surprising that non-uniformity of assessments correlates with underassessment. Both the assessor and property owners are likely to be less aware of deviations from the normal assessment level when values are stated in small fractions of market value than when the values employed approach market value.

⁶ A frequently used argument in the property tax field is that underassessment is not important as long as assessments are at a reasonably uniform fraction of market value. According to this point of view, it makes no difference to the property taxpayer if the tax is 10 mills on 100% of the value or 20 mills on 50% of the value. See Leslie E. Carbert, "Full Value Assessment vs. Fractional Value Assessment," National Tax Association, *Proceedings of the Forty-sixth Annual Conference on Taxation*, 1953, pp. 164-174; and Robert F. Kilmer, "Full Value Assessments: The Legal View," National Tax Association, *Proceedings of the Fifty-first Annual Conference on Taxation*, 1958, pp. 413-420. Those who dismiss underassessment as unimportant sometimes ignore its effects upon the office of assessor, its misrepresentation of the fiscal capacities of local governments—or the need for periodic revision of taxing and bonding limitations—and its correlation with assessment inequities, all of which are discussed in the text below. Moreover, they can only assume the existence of assessment uniformity. Finally, is there any reason to believe that assessments can be kept at a consistent fraction of market value any more readily than at market value itself? Legal assessment at a fraction of market value presupposes the ability initially to establish market value, so why not use the latter as the assessment standard?

⁷ F. John Shannon, "Recent State-Wide Programs to Improve Local Assessments," National Tax Association, *Proceedings of the Forty-fourth Annual Conference on Taxation*, 1951, p. 167.

⁸ Frederick L. Bird, *The General Property Tax: Findings of the 1957 Census of Governments*, 1960, p. 58

This correlation led one analyst of the 1959 Census of Governments to the following conclusion:

It would appear . . . that deep underassessment is a species of built-in hazard in the assessing process. Equality of intra-area assessment, difficult to obtain under most favorable conditions, is much more difficult even to approximate with assessment at minor fractions of full value. There is considerable doubt, for this reason, that the shot-gun-wedding type of legislation now being adopted or urged to make such underassessment legitimate is a sound remedy of inequity.⁹

Among students of the property tax it is common knowledge that this tax has an element of regression in the sense that low value residences are generally assessed at a higher level of their worth than expensive homes. The Census of Governments also reveals a correlation of under-assessment and an increasing degree of regression:

When this regressive tendency is examined at different levels of assessment, it is found to increase as the level of assessment declines. This finding reinforces the disclosure . . . that assessment becomes progressively less uniform as the degree of underassessment increases.¹⁰

The Problem of Uniform Assessments

The need for uniform assessments on individuals of the same class of property is obvious. The need for equal assessments among different classes of property is just as important. When classes as a whole are assessed at different levels, some classes will receive tax windfalls at the expense of others. Since in Montana the various classes of property are not taxed at equal percentages of value, the erroneous conclusion that unequal assessments among classes do not matter is sometimes drawn. Our property classification law is a legal discrimination among classes of property for tax purposes. Nonetheless, it is important that the several classes of property be assessed uniformly before the application of the percentage factors used to determine the taxable value. Otherwise, the result is a serious distortion of the intended effect of the classification law. The law envisages a tax upon 30% of the value of real estate for example, but we have already seen that the census figures reveal the fact that mill levies are actually being applied against approximately 9% of non-farm residential properties and about 7% of farm real estate.

Because a state-wide property tax is levied for state purposes and because state aid to schools is contingent on a minimum local property tax levy, inequities will exist unless property is assessed uniformly not only within counties but among counties. Individual counties might demonstrate a considerable degree of uniform assessments within and among classes of property; but if uniformity does not exist among counties, taxpayers in counties with the higher levels of assessment will pay disproportionate shares of the state levies, and counties with lower levels of assessment are likely to receive disproportionate shares of school aid money.¹¹

⁹ *Ibid.*, p. 59.

¹⁰ *Ibid.* p. 59.

¹¹ In its *Fourteenth Biennial Report* (1950) the Montana State Board of Equalization made the following observation:

The present school finance program requires a district levy of five mills, the county-wide levy of 10 mills for elementary schools, and another county-wide levy of 10 mills for high schools. The amount of state aid hinges on the amount raised by these levels. The smaller the amount raised the greater the amount the state must pay. If property in a county is under-valued, it follows that more state assistance is required. That situation tends to be attractive. Any undeserved aid granted to under-valued districts must be withheld from funds that in fairness should go to other districts. If the recently inaugurated school program should encounter difficulties, it is conceivable that the major trouble will lie in inequality in assessments of real estate and improvements.

INTRA-COUNTY ASSESSMENT UNIFORMITY

Volume V of the 1957 *Census of Governments* provides some data which can be used to indicate the extent of assessment uniformity on real estate in Montana. The data pertain only to the sales of nonfarm houses in 23 sample assessment areas. The data limits analysis to this one class of real estate. Data are not available which would permit a comparison of the extent of assessment uniformity on other types of realty and on personal property. Since the data apply to limited geographic areas, conclusions cannot be interpreted as complete measures of state-wide assessment characteristics for nonfarm houses.

Before an attempt can be made to evaluate the degree of success in achieving assessment uniformity in Montana, it is first necessary to determine what degree of deviation from absolute uniformity is compatible with good assessment. The degree of deviation is measured by the "coefficient of dispersion", which is an index of uniformity; the higher the index the less uniform are assessments. (See footnote 12 for an explanation of how the coefficient of dispersion is determined.) An analysis of the data in the *Census of Governments* and a review of discussions of this question in other tax studies led one author to the following conclusion:

*That one-fifth of all of the 1,263 selected areas were able to show coefficients of dispersion of less than 20 in the assessment of nonfarm houses would seem to indicate that a level of 20 or better for at least this major use class of property is attainable in all assessing areas that are suitably organized and adequately staffed with well-trained assessors. This conclusion is supported by the previously cited determinations of students of assessment administration respecting over-all standards of assessment.*¹²

The coefficients of intra-area dispersion for twenty-three sample assessment areas in Montana are as follows:¹³

Coefficient of Dispersion	Number of Areas
less than 15.0	1
15.0 to 19.9	2
20.0 to 24.9	2
25.0 to 29.9	4
30.0 to 34.9	4
35.0 to 39.9	1
40.0 to 49.9	3
50.0 or more	6

Thus, only three areas fall within the desirable zone of less than 20. Six of the twenty-three areas, or more than $\frac{1}{4}$ of the sample, have coefficients of dispersion of 50 or more. Eighty-seven percent (87%) of the areas fall above 20. The medium for the twenty-three areas is 32.8; for the nation as a whole it is 29.9.

¹² Frederick L. Bird, *The General Property Tax: Findings of the 1957 Census of Governments*, 1960, p. 64. The coefficient of dispersion is determined as follows:

The ratio of assessed value to sales price is determined for each transaction in the sample. The median ratio is then determined. (The median is the mid point of a series arranged according to size.) The deviation in percentage points of each individual assessment ratio from the median is determined. The deviations of each are totaled and averaged by dividing the sum by the number of ratios in the sample. This average is then divided by the median ratio. The result is the coefficient of dispersion.

¹³ From Table 18 in *Taxable Property Values in The United States*, op. cit., p. 88.

The inequities which result where assessment uniformity is lacking are revealed by the table below which shows the tax bills for three houses with a market value of \$15,000. The unequal assessments mean that property owner C pays twice as much as B and four times as much as A. The coefficient of dispersion for the three assessment ratios is 50. While these examples are hypothetical, the census figures indicate that within some Montana counties instances of such gross inequity do exist.

	A	B	C
Assessment ratio	15%	30%	60%
Assessed Value	2,250	4,500	9,000
Tax at 100 mills	\$225	\$450	\$900

INTER-COUNTY ASSESSMENT UNIFORMITY

The Census also provides data on inter-county assessment uniformity on non-farm houses. It must be remembered that the data are based on sample areas and do not, therefore, necessarily represent inter-area inequality for the state as a whole. However, within this limitation, the Census figures reveal that the results for Montana are even more alarming than is the absence of uniform assessments on non-farm homes within the counties. *The coefficient of dispersion of inter-county assessment ratios for the sample is 46, the highest in the nation.* By contrast fourteen states have indexes of 15 or less. Illinois, Indiana, and Wyoming have a coefficient of dispersion of 11, and Oklahoma with 10 is the lowest in the nation. Eight states have indexes of 30 or more. Maine with 42 and Virginia with 40 share with Montana the dubious distinction of having indexes of 40 or more.¹⁴

An analysis of the Census findings explained that in most states with a high degree of inter-area uniformity, inadequate state supervision of local assessment is probably a factor. The author concludes:

*The high indexes of interarea inequality are due to a variety of special causes; but, in general, no satisfactory degree of interarea uniformity is to be expected, in view of the local character of assessment administration, without active state supervision.*¹⁵

AREAS OF PROPERTY TAX REFORM EFFORTS

In its *Sixteenth Biennial Report* (1954) Montana's state board of equalization posed the following question:

No other state has laws that are better, or as well designed to promote an ideal property tax system. Why haven't we got it? (p. 15)

While Montana's tax property laws fall short of being the best in the nation, they are not so inadequate as to be the sole cause of the failure of the property tax program. There is no simple answer to the board's question. If Montana's experience parallels other states', very likely the breakdown has occurred at all levels of the assessment system.

¹⁴ Table 17 in *Taxable Property Values in the United States*, op. cit., p. 87. In its *Fifteenth Biennial Report*, (1952), the State Board of Equalization commented on the absence of uniform assessments on real estate as follows:

Property is now, and probably will be for many years, the principle and most dependable source of revenue for Montana counties, schools and municipalities. Our constitution requires, and common sense demands, that it be uniformly assessed. That objective has been substantially met in the assessment of livestock and all other major classes of personal property, but in the assessment of real estate and improvements there is practically no uniformity on a state-wide basis. (p. 3)

¹⁵ Frederick L. Bird, *The General Property Tax: Findings of the 1957 Census of Governments*, 1960, p. 64.

Assessment of Utilities

The Council has not attempted to determine whether or not specific utilities are paying their fair share of taxes. This part of the report is primarily designed to raise questions about utility appraisal methods in general and about the board's method in particular.

In the vast majority of the states some kinds of utilities are assessed for property taxation by central state agencies. In Montana central assessment of inter-county railroad property is provided for in the constitution. The statutes provide for a central assessment of other kinds of inter-county utility property.

In appraising utilities many state agencies, as does Montana's state board of equalization, employ what is known as the unit rule of appraisal—the appraisal of property as a whole without regard to its constituent parts. This method is used because the individual properties which make up a utility unit can produce income only if they are parts of a functioning whole; therefore, the value of the functioning unit may be more than the sum of the cost of individual parts of the unit.

The board shares assessment of utility property with the 56 county assessors who assess operating property such as furniture and fixtures, depots and other buildings which are located in their counties. The board arrives at its valuations to be allocated to the counties by subtracting the sum of all such locally-assessed property from its total assessment of the operating property of the entire utility. Therefore, no matter how high or low the level of county assessment, the total assessed value of the utility will always be no more and no less than the board's unit appraisal.

It seems inconsistent with the unit rule of appraisal to apportion utility valuations on the assumption that county assessors can accurately appraise individual properties which the board by its appraisal process views as integral parts of an operating unit.

Because of Montana's property classification law, locally assessed property of utilities is placed in several classes ranging from 7% to 40% while values allocated by the board are all taxable at 40%. While the total assessed value of the utility will always be what the board has determined it to be, the greater the total local assessment the less the taxable value will be. However, a utility's total tax bill will not necessarily be reduced because the lower taxable value may be more than compensated for by the crediting of taxable valuations to taxing districts with high mill levies.

Since each part of the utility unit is necessary to the proper functioning of the whole, it seems inconsistent to treat utility valuations as one class of property when they are allocated by the board of equalization, but as another class when they are appraised by the county assessor.

In making its unit appraisals the Montana state board of equalization considers three factors: capitalized net earnings, total stock and bond value, and original or reproduction plant cost. The assessed value of the utility is generally arrived at by an average of these three factors.

To determine the income figure to be capitalized, the appraiser must critically evaluate a utility's accounts so as to include all operating income. The next step is to average the earnings for a specified period of time. In Montana the state board of equalization employs in each case a non-weighted five-year average of earnings. Tax authorities agree that if a period average is employed the more recent years should be weighted for those utilities which are evidencing consistent growth. The Montana state board of equalization capitalizes income at the rate of 6%. This rate appears to be based on nothing more than a tradition. Rates of capitalization should vary depending on the utility or type of utility. The rate of capitalization is important because only a slight difference in the rate can mean a considerable variance in final assessment.

Montana's board of equalization also employs market value of stocks and bonds as an evidence of value in appraising railroads and major utilities. The method, based on the accounting maxim that assets equal liabilities, is used to value a utility's assets by determining the value of its liabilities. However, if the value of stocks and bonds is to be a valid indicator of value, the volume of trading must be sufficient to justify its use. The board of equalization uses a five-year average of prices quoted on December 31 preceding assessment day. A five-year average of stock and bond prices is subject to the same criticism applied to long-term averages for net earnings. Some authorities have suggested an average of prices for periods of six months to a year.

The state board of equalization considers original cost, apparently with some allowances for depreciation, in assessing utilities other than the railroads. The board uses reproduction costs new less depreciation in appraising railroads. The relevance of plant cost figures largely depends upon what plant costs rate-making bodies will accept in establishing rate bases. Since the Montana Public Service Commission considers depreciated reproduction cost, original cost and depreciated original cost in establishing rate bases, the board of equalization should consider giving some weight to all three in appraising those utilities whose rate bases are determined by the public service commission. The board's use of reproduction costs new less depreciation in appraising railroads appears questionable because the earnings of railroads bear little relationship to plant costs.

The board's system of averaging capitalized earnings, stock and bond value and plant costs will not automatically result in accurate valuations when it is indiscriminately applied in all cases. Authorities agree that a mechanical application of a formula combining the evidences of value is not likely to result in accurate assessments since each utility is unique.

The Council does not conclude that the board's utility appraisal methods are necessarily "wrong" or that inaccurate results have been attained. However, it does seem fair to say that the board has devoted little energy to a continuing, critical examination of its methods.

Equalization of Utility Assessments

In 1959 the state board of equalization reduced the assessed value of the major utilities alone by almost \$35,000,000. The reduction is partially reflected in the net loss of over \$9,000,000 in the taxable value of utilities between 1958 and 1959.

The board maintains that its reduction of utility assessments was necessary as an equalization measure. The justness of the action hinges on the board's contention that the state-wide average level of assessments for all types of locally assessed property is 35 to 37% of true value and that their own assessment of utilities averages some twenty percentage points higher than this. The board's 35 to 37% assessment level figure is largely based upon real estate sales ratio studies conducted by some of the larger utilities owning property in the state.

To yield reliable results, sales ratio studies must be conducted carefully and in accord with clearly defined procedures. The sampling, weighting and classification techniques employed by the utilities and the board appear to be somewhat deficient.

Court testimony of a board member in the case of Yellowstone Pipeline Company and Oil Basis Pipeline Company vs. the State Board of Equalization and the brief of the board's attorney indicate that the board itself appears unwilling to vouch for the accuracy of the sales ratios furnished by the utilities and published in its own 17th biennial report.

The board's duty to equalize is specific and mandatory. The gathering of facts on assessments within and among counties by sales ratio studies, or by some other method, is an inseparable part of the board's duty to equalize. Delegation of responsibility for com-

piling and interpreting such data to private corporations with a direct pecuniary interest in the results cannot be regarded as proper and can only result in embarrassment to both the board and the utilities.

The manner in which the sales ratio studies were conducted casts doubt on the validity of their results and it appears that statements by board members on the assessment level of personal property as a whole cannot be supported by data gathered in any systematic manner. Because the board's figure of 35-37% as a state-wide average level of assessment for local assessed property cannot be defended, neither can the board's reduction of utility assessments.

While the board reduced utility assessments in an attempt to equalize among different classes of property, it has not equalized among utilities themselves. By the board's own admission, in 1959 major utilities were assessed from 65.5% to 46.5% of full value and railroads were assessed from 74.8% to 34.35%.

Organization of State Tax Department

Most of Montana's taxing activities are concentrated within one department, the state board of equalization. The powers and duties of the board of equalization can be divided into five broad categories. They are:

1. *Collection* of all taxes for state purposes.
2. *Supervision* of county assessors and county boards of equalization.
3. *Assessment* of certain classes of property for state and local purposes.
4. *Equalization* of the valuation of taxable property among counties, classes of property and between taxpayers.
5. *Review* of specific assessments on its own initiative or by hearing appeals from the findings of county boards of equalization as well as appeals from its own assessment of inter-county properties.

Thus, the title "Board of Equalization" is not truly descriptive of the many duties performed by this board.

Conclusions

A general trend in state government away from multi-headed agencies is reflected in the area of taxation. Thirty-five of the fifty states have provided a single administrator for their principal taxing agencies. In Montana the state board of equalization is the only board devoting full time to administering a department.

There are several apparent reasons why a single administrator would be superior to a board.

1. A board of equalization can be justified in only a relatively small area of the property tax field.
2. It is offensive to our concept of justice for a board to hear appeals from its own administrative rulings.
3. It is inefficient to vest responsibility for the management of a department in a board rather than in a single administrator.

Recommendations

The Council recommends that the Montana constitution be amended so as to delete all reference to the board of equalization. This would not abolish the state board of equalization—the board would continue to function under statutory authority. The legislative assembly, at a future date, could consider the establishment of a single tax commissioner.

The organization of the New Jersey tax department illustrates a possible plan for organizing a tax department in the future.

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MONTANA CONSTITUTIONAL CONVENTION

1971-1972

TAXATION AND FINANCE

By ROGER A. BARBER

CONSTITUTIONAL CONVENTION STUDY NO. 15

PREPARED BY

MONTANA CONSTITUTIONAL CONVENTION COMMISSION

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process, from Step 1 (determining the full cash value of property) to Step 4 (computing the actual amount of taxes owed):¹⁰

- Step 1: \$25,000 residence at market or full cash value (appraised value)
- Step 2: \$25,000 (appraised value)
x 40%
\$10,000 (assessed value)
- Step 3: \$10,000 (assessed value)
x 30% (determined by classification law)
\$ 3,000 (taxable value)
- Step 4: \$ 3,000 (taxable value)
x256.01 mills (mill figure will vary from place to place. It represents total property taxes for state, county, municipal, school and special district purposes in each area.)
\$768.03 (property tax bill)

With this four-step process in mind, the actual workings of the property tax system can be examined.

Underassessment and Uniform Assessment

Two major and almost universal problems of property tax administration are underassessment and the lack of uniform assessment. When used in this context, "assessment" means determining the actual or cash value of property, and not the more particularized meaning assigned the term under Montana taxation procedures. In other words, underassessment results when property is appraised at less than the level required by statute. Absence of uniform assessment exists when all classes of property within a taxing jurisdiction are not appraised at the same level.

Underassessment

The Montana Legislative Council in a 1960 study concluded that property in Montana is greatly underassessed:

The Census shows Montana's assessment of real property as 8% of its value as indicated by sales prices;

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however, this figure was determined by using taxable value rather than assessed value. The figure reflects, therefore, not only the performance of the assessor but the effects of our property classification law as well. The combination of underassessment and our classification law means that mill levies are applied to only about 8% of the market value of real estate.

The performance of the assessors can be more accurately demonstrated by adjusting the Census figures to show assessed values as a percent of sales prices. This reveals that in Montana non-farm residential property is assessed from 28.7% to 31.7% of its sales value.¹¹

Several factors contribute to underassessment, according to the Council:

1. Assessments are slow to respond to price increases in the money market. For instance, real property is frequently assessed at its value several years ago and does not reflect current increased valuations.

2. Assessors are tempted to underassess to benefit their counties.

Where the state imposes a property tax levy or where state aid to schools is apportioned on the basis of yields from fixed mill levies, assessors are under considerable pressure to compete among themselves for underassessment. By assessing at less than the average level, the county assessor can shift state property taxes to other counties and increase apparent need for state aid to schools.¹²

3. The assessor, as an elected official, can use underassessment as an election tool.

The assessor, who among all local officials receives the most complaints about taxes, can use underassessment to parry them. Because the individual will often consider himself as having received a "break," underassessment is popular with property owners. This is an important consideration to a man who must retain his office through election.¹³

4. The assessor can also shift the responsibility for increased taxes.

The assessor may wish to keep assessments in line with price increases, but he knows that if he does so

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and local governing agencies fail to decrease mill levies, protest as he might, he will probably incur public wrath for tax increases. If he can hold the line on assessments and local legislative bodies are forced to resort to increased mill levies, responsibility for tax increases will be shifted to them.¹⁴

Perhaps the most damning indictment against underassessment is that it turns the county assessor into a one-man legislature.

For example, in Montana salaries of many local officials are tied by statute to population and taxable valuation of counties. By assessing at less than the legal limit, the assessor alters the effect of these statutes and reduces the salaries of some officials. Similarly, fractional assessments also alter existing statutory taxing and bonding limitations by making them more restrictive than contemplated by law. This misrepresents the fiscal capacities of local governments and leaves some of them with little or no financial elbow room.¹⁵

An index has been formulated to determine the degree of deviation from the absolute uniformity compatible with good assessment. The degree of deviation is measured by the coefficient of dispersion, which is an index of uniformity. The higher the index, the less uniform are assessments.

The 1960 Legislative Council study reported the coefficients of intra-area dispersion for twenty-three sample assessment areas in Montana were as follows:

<u>Coefficient of Dispersion</u>	<u>Number of Areas</u>
less than 15.0	1
15.0 to 19.9	2
20.0 to 24.9	2
25.0 to 29.9	4
30.0 to 34.9	4
35.0 to 39.9	1
40.0 to 49.9	3
50.0 or more	6

PROPERTY TAX

The Council noted:

[O]nly three areas fall within the desirable zone of less than 20. Six of the twenty-three areas, or more than 1/4 of the sample, have coefficients of dispersion of 50 or more. Eighty-seven percent (87%) of the areas fall above 20. The medium for the twenty-three areas is 32.8; for the nation as a whole it is 29.9.¹⁶

In a study based on figures prepared by the Bureau of the Census in 1967, one writer concluded "a reasonable degree of uniformity of assessment exists within counties, but a serious absence of uniformity exists between counties."¹⁷ That writer said:

Assessment for 10 selected areas showed an average uniformity of 22.5 percent within counties, as compared with the national average of 19.2 percent, measured in terms of the coefficient of intra-area dispersion. But data on inter-county assessment uniformity showed an average uniformity of 43.0 percent, tying New Hampshire and Texas for the highest in the nation.¹⁸

Part of the poor record in intercounty uniformity probably can be traced to reasons discussed earlier. Some county assessors may deliberately under-value property to gain tax breaks and larger portions of state aid.

Non-uniformity of assessment is a violation of the Equal Protection Clause of the United States Constitution. In Sioux City Bridge Co. v. Dakota County,¹⁹ the U. S. Supreme Court held that a taxpayer whose property had been discriminatorily assessed at full value must be granted a reduction to the fraction at which other parcels had been assessed. The discrimination must be more than incidental to violate the Equal Protection Clause, however.

This discussion of the major problems facing the assessment function reveals the political power wielded by the assessor. His day-to-day decisions have enormous consequences.

County Assessors

Article XVI, Section 5 of the Montana Constitution requires that an assessor "shall be elected in each county" and shall possess the qualifications for suffrage prescribed in Article IX, Section 2, and such other qualifications set by law. The constitutional suffrage qualifications are: at least 19 years old; United States citizenship; residency within the state for at least a year; residency within the